

Message Text

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PAGE 01 OECD P 30393 211140Z

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-07

EA-07 FRB-03 INR-07 IO-10 NEA-10 NSAE-00 OPIC-03

SP-02 TRSE-00 CIEP-01 LAB-04 SIL-01 OMB-01 SSO-00

INRE-00 NSCE-00 /075 W

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O 211123Z NOV 75

FM USMISSION OECD PARIS

TO SECSTATE WASH DC IMMEDIATE 9345

INFO AMEMBASSY HELSINKI IMMEDIATE

LIMITED OFFICIAL USE OECD PARIS 30393

E.O.11652: N/A

TAGS: ECON, OECD

SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC)
ANNUAL REVIEW OF FINLAND, NOVEMBER 24, 1975

REF: OECD DOCUMENT EDR(75)29

1. BACKGROUND AND SUMMARY: IN REFDOC CIRCULATED IN PREPARATION FOR NOVEMBER 24 EDRC REVIEW OF FINLAND, SECRETARIAT NOTES THAT FINLAND MAINTAINED A HIGH LEVEL OF ACTIVITY IN 1974. THE UNEXPECTEDLY SHARP INCREASE IN EXPORT PRICES COUNTERACTED THE IMPACT OF THE OIL PRICE RISE ON FINLAND'S TERMS OF TRADE, AND AT THE SAME TIME ADDED TO DOMESTIC DEMAND PRESSURES. IN PARTICULAR, PRIVATE FIXED CAPITAL FORMATION REMAINED PARTICULARLY BUOYANT. REFLECTING THE STRONG DEMAND PRESSURES, HOWEVER, A GROWING DEFICIT EMERGED ON THE CURRENT ACCOUNT OF THE BALANCE OF PAYMENTS, WHILE THE RATE OF INFLATION ACCELERATED. BY THE LATTER PART OF 1974 SIGNS OF A CLEAR SLOWING DOWN IN THE GROWTH RATE OF OUTPUT BECAME EVIDENT, WHICH CONTINUED INTO 1975. NEVERTHELESS, THE CURRENT ACCOUNT DEFICIT CONTINUED TO GROW, LEADING THE LIMITED OFFICIAL USE

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PAGE 02 OECD P 30393 211140Z

AUTHORITIES TO INITIATE A SERIES OF RESTRICTIVE MEASURES

AIMED AT REDUCING DEMAND PRESSURES AND ESPECIALLY THE FLOW OF IMPORTS. DESPITE A SLOWING DOWN IN DOMESTIC DEMAND, A SIZEABLE DETERIORATION IN THE REAL FOREIGN BALANCE IS EXPECTED TO LEAD TO A FALL IN GDP THIS YEAR. FOR 1976, THE PROSPECTS ARE FOR A STAGNATION IN OVERALL OUTPUT, WITH AN ACTUAL DECLINE IN THE VOLUME OF TOTAL DOMESTIC DEMAND BEING COUNTERBALANCED BY A TURNAROUND IN THE REAL FOREIGN BALANCE.

2. POLICY: THE FISCAL CONCESSIONS MADE TO ENSURE THE SIGNING LAST YEAR OF A CENTRALIZED INCOMES SETTLEMENT REDUCED THE FLEXIBILITY OF BUDGETARY POLICY. UNDER CONDITIONS OF STRONG DOMESTIC DEMAND, COMMERCIAL BANK BORROWING IN THE CENTRAL BANK AND ABROAD HAD BEEN CONSIDERABLE. POLICY HAS SWUNG OVER TO A MORE RESTRICTIVE STANCE SINCE EARLY 1975. MEASURES TO RESTRAIN THE GROWTH OF PUBLIC EXPENDITURE HAVE BEEN ANNOUNCED, THOUGH THEIR REALIZATION WILL IN MANY INSTANCES BE SUBJECT TO CONSIDERABLE LAGS. IN THE MONETARY FIELD THE COMMERCIAL BANKS' BORROWING QUOTAS HAVE BEEN REDUCED AND GREATER RESTRICTION ON FOREIGN BORROWING ANNOUNCED. SECRETARIAT CONCLUDES, HOWEVER, THAT IF THE PRESENT POLICY OBJECTIVES OF REDUCING THE CURRENT ACCOUNT DEFICIT AND THE RATE OF INFLATION ARE TO BE ATTAINED, A CONTINUED TIGHT POLICY STANCE TOGETHER WITH MARKED INCOME RESTRAINT WILL BE REQUIRED.

3. IN LIGHT OF ABOVE DISCUSSION OF PROSPECTS AND POLICIES, SECRETARIAT EMPHASIZES NEED FOR MORE EFFECTIVE MONETARY MANAGEMENT (ESPECIALLY IN LIGHT OF POSSIBLE RAPID INCREASE IN LIQUIDITY IN MARCH, 1976, WHEN IMPORT DEPOSIT SCHEME SCHEDULED TO BE LIFTED). SECRETARIAT ALSO RECOMMENDS IMPROVING EFFECTIVENESS OF CENTRALIZED WAGE AGREEMENTS AND IMPLEMENTATION OF TEMPORARY BUT STRICT PRICE CONTROLS.

4. COMMENTS: DURING EDRC REVIEW MISSION INTENDS SEEK TO ELICIT REITERATION OF FINNISH INTENTION TO REMOVE IMPORT DEPOSIT REQUIREMENT IN MARCH, 1976 BY QUESTIONING FINNS ABOUT BALANCE OF PAYMENTS AND DOMESTIC MONETARY LIMITED OFFICIAL USE

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PAGE 03 OECD P 30393 211140Z

EFFECTS OF DOING SO. REFDOC NOTES THAT SUBSTANTIAL SHORT TERM CAPITAL INFLOWS IN 1974 (MAINLY PREPAYMENTS BY GOVERNMENTS FOR FUTURE FINNISH EXPORTS) HAVE HELPED TO LOWER BURDEN OF SERVICING LONG-TERM DEBT AND TO FINANCE LARGE CURRENT ACCOUNT DEFICIT. THIS SHORT-RUN STRATEGY COULD HAVE ADVERSE CONSEQUENCES OVER MEDIUM-TERM ON CURRENT ACCOUNT AND DEBT SERVICE BURDEN. MISSION INTENDS TO POSE GENERAL QUESTION TO FINNS ON IMPLICA-

TIONS OF THIS STRATEGY.

5. ACTION REQUESTED: MISSION WOULD WELCOME COMMENTS/
QUESTIONS WHICH DEPARTMENT OR EMBASSY HELSINKI MIGHT
HAVE RE SECRETARIAT RECOMMENDATIONS AND MISSION COMMENTS
PARA 4.
TURNER

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC DEVELOPMENT, ECONOMIC CONDITIONS, INFLATION
Control Number: n/a
Copy: SINGLE
Draft Date: 21 NOV 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: CunninFX
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975OECDP30393
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D750406-0128
From: OECD PARIS
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t19751120/aaaaarsh.tel
Line Count: 122
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EUR
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: CunninFX
Review Comment: n/a
Review Content Flags:
Review Date: 13 MAY 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <13 MAY 2003 by izenbei0>; APPROVED <02 OCT 2003 by CunninFX>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
06 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC) ANNUAL REVIEW OF FINLAND, NOVEMBER 24, 1975
TAGS: ECON, OECD
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 06 JUL 2006